This record is a partial extract of the original cable. The full text of the original cable is not available.

UNCLAS SECTION 01 OF 02 PARIS 001050

SIPDIS

PASS FEDERAL RESERVE
PASS CEA
STATE FOR EB and EUR/WE
TREASURY FOR DO/IM
TREASURY ALSO FOR DO/IMB AND DO/E WDINKELACKER
USDOC FOR 4212/MAC/EUR/OEURA

E.O. 12958: N/A
TAGS: EFIN ECON PGOV FR PBIO
SUBJECT: GDP INCREASED 2.3 PERCENT IN 2004; UNEMPLOYMENT
REMAINED HIGH

¶1. SUMMARY. According to the latest flash estimate, French GDP increased a relatively high 2.8 percent (annualized) in the fourth quarter of 2004, which means France posted a decent 2.3 percent growth rate for 2004. Domestic demand revived, contributing to significant import growth. France posted a small foreign trade deficit as exports increased less than imports. Despite 2.3 percent GDP growth, the unemployment rate remained stubbornly stuck at 9.9 percent. In response, the GOF announced measures to boost economic growth and reduce significantly unemployment in 2005, to be reported septel. END SUMMARY.

GDP increased 2.3 percent in 2004

¶2. Based on a National Institute for Statistical and Economic Studies (INSEE) flash estimate, economic growth recovered in Q-4 as GDP increased 2.8 percent (annualized), after stagnating in Q-3. Including an upward revision in both Q-1 and Q-2 GDP to 2.8 percent from 2.4 percent, full-year growth came in 2.3 percent, despite the Q-3 break, or 2.5 percent non-adjusted for worked days. The 2004 performance, which is far better the 0.5 percent growth in 2003, came in above the expected 2.2 percent growth, but remained below the 2.5 percent GOF forecast. Finance Minister Gaymard rounded 2004 GDP growth to "about 2.4 percent" in his February 8 speech on the GOF economic policy in the next 30 months.

Domestic demand was the Main driver

¶3. Gaymard credited the strength in growth rates to a Q-4 boom in consumer spending. The Finance Minister said that consumer spending growth accelerated to 2.2 percent from 1.6 percent in 2003 despite the correction that stalled the economy in Q-3. Price discounts and various temporary tax breaks (cutting inheritance and gift taxes, and permitting early withdrawal from corporate savings accounts) helped boost spending in Q-4. More than 2 million people withdrew 5.6 billion euros from employee-savings. The inheritance incentive resulted in the transfer of 5.4 billion euros between June and December. Housing investment accelerated in France, increasing 3.7 percent.

¶4. The long-awaited recovery in corporate investment finally took place in 2004. Corporate investment rebounded 2.9 percent (excluding inflation), after decreasing 1.6 percent in 2003.

--- -----
Exports Rebounded, but Increased Less than Imports
--- -----

¶5. The French trade balance (Fob/Fob - Customs basis) registered a 7.8 billion euro deficit (0.4 percent of GDP) in 2004 compared with a 1.7 billion euro surplus in 2003. Exports increased (5.6 percent) less than imports (8.6 percent). Companies argued the strength of the euro made export business difficult. The sharp increase in imports was mainly due to a rise in domestic demand and imported commodity prices, notably oil prices.

¶6. Gaymard confirmed that the rise in imports reflected strong domestic demand. Foreign Trade Minister Francois Loos underlined that "both exports and imports reached record highs, the result of strong internationalization of the French economy." Answering implicitly commentators who said that French exports lost competitiveness since world trade increased 12 percent in 2004, Loos stressed "there was no competitiveness problem since the French foreign trade excluding the energy deficit (28.9 billion euros) posted a surplus."

¶7. On a geographical (CIF/FOB) basis, France posted a

deficit with the euro zone (6.6 billion euros) in 2004, notably a significant trade deficit with Germany, its major trading partner (11.5 billion euros). France had a surplus with the 15 EU members (1.6 billion euros), and the 25 EU members (3.2 billion euros). With the U.S., France posted a 1.1 billion euro surplus.

Despite Oil Prices, Inflation was Moderate

¶7. In December, the year-over-year consumer price increase was moderate (2.1 percent), notably because oil prices dropped to USD 43.45 a barrel at year's end from a record high of USD 55.17 on October 22. The increase in consumer prices excluding oil prices was 1.5 percent, probably reflecting the on-going impact of the Government "arm-twisting" on distributors to cut retail prices. Price increases in the services sector were less moderate (2.6 percent).

-- ----------
Weakness: Unemployment Rate Stuck at Around 10 percent
-- ----------

¶8. The unemployment rate remained high at 9.9 percent in December, twice the unemployment in some other European countries as the French economy only created 40,000 jobs in ¶2004. The GOF pledges to steer joblessness below 9 percent in 2005 by reducing the number of unemployed by 10 percent through the net creation of 200,000 to 300,000 jobs.

-- -----
GDP Growth Could Be Lower than 2.5 percent in 2005
-- -----

¶9. Q-4 GDP growth was better-than-expected. Many private-sector economists had forecast 2.4 percent (annualized). In January, economists forecast 2005 GDP growth to slow to 1.8 percent, below a potential trend of 2.25 percent, notably fearing a renewed weakness in consumption in early 2005 due to high unemployment that contributes to household pessimism and amplifies the vicious circle of lower demand and fewer job creation. Recently, the Bank of France forecast GDP to increase 2.0 percent (annualized) in Q-1 2005, taking into account recent INSEE's estimate of Q-4 GDP growth, and indications provided by its business climate indices for January.

-- --------------
Comments: Achieving 2.5 percent GDP Growth in 2005 Remains Unsure
-- --------------

¶10. France's 2004 GDP performance was no so bad, as GDP growth outpaced other large euro zone countries, notably Germany. That said, the GOF is aware that achieving its 2.5 percent GDP growth objective in 2005 and reducing significantly unemployment will be hard to achieve without further measures and reforms. In his February 8 speech, Gaymard announced a series of measures to boost economic growth and eliminate the vicious lack-of-confidence circle by stimulating consumer spending, the purchasing power and activity of companies, and thus job creation. The GOF policy will be reported septel.
LEACH